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SUBJECT: ECONOMIC SLOWDOWN PUTS THE BRAKES ON SHIPPING TRAFFIC IN THE
YANGTZE RIVER DELTA

REF: A. A) 08 BEIJING 4679
¶B. B) GUANGZHOU 009
¶C. C) BEIJING 443

(U) This message is sensitive but unclassified.

¶1. (U) Summary: Previous unrestrained growth in the Yangtze River Delta has left the shipping industry making unprecedented decisions to cut costs, shift assets, and survive during the economic downturn. Shipping companies have dramatically cut rates and some are operating at below cost, further driving down any short-term profitability. Compared to South China, industry experts say it is not all gloom in East China with some container shipments and bulk traffic supporting port activity. The Yangtze River Delta is doing comparatively better than South China, according to East China shipping industry participants. End Summary.

## Port Traffic Cooling Down

¶2. (SBU) Two of the top ten ports in the world are found in the Yangtze River Delta, Shanghai and Ningbo, making the region's ports a key bellwether of world trade activity. Container port traffic has contracted considerably across all ports in the Yangtze River Delta covering Shanghai (Yangshan and Waigaoqiao), Ningbo, Zhoushan, and Lianyungang. The Yangshan Deepwater port, although capable of impressive loading rates at almost 700 twenty-foot equivalent units (TEU) per hour, is currently operating at 20 percent below capacity. On a mid-February visit to Yangshan Port, which handles 60 percent of Shanghai's volume, Econoff noticed that there were no cargo containers being loaded, unusual for a busy port where 24 hour operations have been commonplace to keep with annual double-digit growth. Port officials said that shipments had dropped by 30 percent since their peak in 2008. Yangshan Port General Manager Jiang Gongsheng told Econoff that he is running two instead of three work shifts, and many employees are assigned to training during this downturn. Yangshan typically services four shipments a week for the Middle East and European trade lanes. The other major Shanghai port, Waigaoqiao, which currently handles the vast majority of U.S.-bound cargo originating from or transiting

through Shanghai, has also seen similar reductions in traffic volumes. More strikingly, Lianyungang in northern Jiangsu Province, China's ninth largest port in TEU handled in 2008, had no noticeable container ships berthed for loading, minimal container truck activity, and noticeably open berth side container yard space during a March 3 site visit.

Lower Commodity Prices Pushing up Bulk Volumes
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¶3. (SBU) Lianyungang port authorities on March 3 nonetheless maintained that the drop in export demand from the world economic crisis has not affected overall port activities on a large scale. Ports in the YRD region are showing a steady growth of bulk commodity imports fueled by domestic demand for raw materials and natural energy resources due to higher levels of government spending for infrastructure projects, according to a recent report from Cargonews Asia. (Note: Oil prices have dropped since December 2008, instigating a rush to purchase and stockpile oil at cheaper prices; see ref B. End note.) The Shanghai ports are continuing to process ships loaded with coal, crude oil, iron ore, and other natural resources for further use in upriver provinces and municipalities all the way to Chongqing. Bulk dry cargo in the area has grown on average at 17.2 percent annually for the past 10 years, but industry experts are expecting a slower growth rate of 8.2 percent in ¶2009.

Shippers Preparing for the Worst, but Optimistic



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¶4. (SBU) Ocean freight forwarders, who are the first to analyze shipping orders coming through the manufacturing pipeline, claim that shipping companies' drop in revenue during the last quarter of 2008 was not a complete surprise. Signs of the decrease in demand were seen at the end of second quarter 2008. Particularly troubling, however, are the rates at which ocean freight revenues and volume plummeted in the beginning of fourth quarter 2008, reports William Chan, Vice President of American President Lines (APL) Logistics China. According to Chan, certain shippers in the region were offering container rates below cost just to fill up capacity commitments.

Rock Bottom Prices for Containers, but Still no Cargo
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¶5. (SBU) December and January cargo rates fluctuated as demand was dropping and capacity was taken out of use to stabilize prices. Even so, cargo rates dropped on a weekly basis in February across all trade lanes. The price of one transpacific container which at times in 2008 cost USD 1200 plus additional fuel and other surcharges has dropped down to two to three hundred USD with all surcharges included. Despite price incentives like reduced fuel costs, renegotiated contract rates, and lower ad hoc rates to move cargo, according to Juan Bautista, Asia Headquarter General Manager of Werner Global Logistics, there is no freight to move.

Not Doing Well, but Better than the Pearl River Delta
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¶6. (SBU) Bautista also pointed out that the Chinese New Year peak shipping season for container export cargo started earlier this year which may skew overall year on year figures, but many factories in the YRD area have been on hiatus since December 2008 to February 2009 with no major activity in sight. Companies that were once aggressively competing for space to move their cargo during the three peak seasons, Back-to-School,

Christmas, and pre-Chinese New Year, are not expecting any peak seasons at all in 2009. However, shippers in the East China region all agree that they are not doing as well compared to the Bohai Bay in the North, but are confident that the Yangtze River Delta market is certainly doing better than the Pearl River Delta market (refs A and B). APL's Chan believes that the container shipping industry as a whole will show signs of recovery in 2010.

Playing Risky Roulette in the Shipbuilding Industry
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¶7. (SBU) More than half of China's shipbuilding industries are concentrated in Shanghai, Jiangsu, and Zhejiang areas in terms of the number of shipyards in the area. In recent months, the industry has been faced with surpluses of ship inventories where there once were heavy backlogs. Chinese shipbuilders produced on the assumption there will always be demand for capacity out of China, an environment of unfaltering and continuous growth. (Note: With average five-year timelines from order to ship delivery, the shipbuilding market is a very risky, capital intensive industry. Compared to other shipbuilding countries, China is even more speculative due to port development in parallel with ship building orders; see ref C. End note.)

Avoiding Losses at All Costs
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¶8. (SBU) Ship owners' responses, although varied, are aimed towards cost-cutting measures minimizing losses from speculative orders for new ships placed up to 5 years ago. Shipbuilders in East China are seeing common cost-cutting responses such as delays in orders or earlier retirement of existing ships. What was once unheard of before, some shippers are choosing last-resort measures like order defaults (with time delays built in for court proceedings) or cancelling new builds, both exceptionally costly options.



Shifting Ship Inventories
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¶9. (SBU) APL, one of the largest shipping lines in China, saw ship utilization capacity fall to 83 percent in fourth quarter ¶2008. While dealing with the drop in demand for cargo space, APL is also facing twenty-eight new vessel commitments due from 2009 to 2012. According to APL's Chang, the thirteen ships committed for delivery in 2009 will replace ships that will be forced into early retirement while the remaining contracts have been negotiated for delivery in 2010 and 2012. During February meetings with China Shipping and COSCO, two of the largest Chinese state-owned shipping companies, company executives report no slowdown in growth plans in spite of the drop in demand. COSCO's Cosco Shipbuilding subsidiary even plans to expand ship repair and conversion operations opened in 2008 in Lianyungang to facilitate shipbuilding operations in the near to medium term. (Comment: Ship order activities are matters that fall into sensitive company internal information. China Shipping and COSCO offered conflicting information compared to industry observers in regards to the existence or number of cancelled or delayed ship orders. End Comment) (Note: China's economic stimulus plan will directly support the shipbuilding industry. Stimulus plan directives for the shipbuilding industry include: supply domestic ship line demand with domestic products, encourage scrapping of aged ships and buying of more new ships, offer financing for new ships, adjust export tax rebates, and consolidation in line with the automobile manufacturing and steel industries. For details see ref C. End note.)

What Happened to the Unused Capacity Space?
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¶10. (SBU) In describing the unprecedented changes to the market in recent months, Jannson Chan, ocean freight director of DSV Air and Sea, noted that 800,000 TEU, equivalent to 100 fully loaded container ships, were pulled from the entire China market ship capacity this January in an attempt to boost rates slumping from overcapacity. Anecdotal information from an executive from APM Terminals and Shanghai maritime safety officials reveals that hundreds of laid up vessels are anchored at sea near ports in Singapore, the Philippines, and Shanghai and Ningbo. Empty containers have been stored since Chinese New Years on unused vessels to save demurrage fees. In Lianyungang, where China Shipping has a large joint venture that manufactures containers, unused new containers numbering in the thousands can be seen from the main highway, stacked seven containers high - taller than the factory building in which they were made and laid out across company property and on nearby open lots. That container factory has at least temporarily ceased production and workers are currently just receiving a minimal monthly payment (shenghuo fei) to avoid unemployment and the possibility of social unrest, according to Lianyungang municipal officials speaking in early March.
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